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JOEY R. FLOYD, P.A.
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LEAH EDWARDS GARLAND

March 5, 2009

The Honorable Charles L.A. Terreni
Chief Clerk/Administrator
Public Service Commission of South Carolina
101 Executive Center Drive
Columbia, South Carolina 29210

RE: Annual Review of Base Rates for Fuel Costs of South Carolina Electric & Gas Company; Docket No. 2009-2-E

Dear Mr. Terreni:

CMC Steel South Carolina ("CMC Steel") is hereby filing with the Public Service Commission of South Carolina ("Commission") twenty-five (25) copies of the direct testimony and exhibits of its witness Richard Thomas in the above-referenced matter. As part of the direct testimony of Mr. Thomas, CMC Steel is filing both a public and confidential version of the testimony and exhibits. The confidential version is filed in a separate and sealed envelope.

During the pendency of this matter, CMC Steel requested, and South Carolina Electric & Gas Company ("SCE&G") provided pursuant to the terms of a Confidentiality Agreement ("Agreement"), certain documents which SCE&G asserts are proprietary, commercially and/or competitively sensitive or confidential or in the nature of a trade secret ("Confidential Information"). As part of the Agreement, CMC Steel agreed to safeguard such information so as to prevent disclosure to any unauthorized person(s). To the extent that it desires to use any of the Confidential Information as part of any filing, argument, or hearing in this proceeding, CMC Steel agreed to work with SCE&G to establish a procedure designed to protect the Confidential Information from disclosure to any unauthorized person(s).

In keeping with the terms of the Confidentiality Agreement, CMC Steel and SCE&G have discussed CMC Steel's desire to use certain Confidential Information in this proceeding and have agreed that CMC Steel will file a public and confidential version of the direct testimony, including any exhibits, of Mr. Thomas. I am informed that SCE&G plans to file a Motion for Confidential Treatment asserting that the testimony contains protected information and requesting that the Commission issue a protective order protecting the Confidential Information from disclosure. I am further informed that SCE&G's motion will cite as authority for protecting the Confidential Information S.C. Code Ann. Regs. 103-804(S) and 103-829, the South Carolina Freedom of Information Act, S.C. Code Ann. Section 30-4-10 *et seq.* and other

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The Honorable Charles L.A. Terreni

March 5, 2009

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applicable law. Therefore, CMC Steel respectfully requests that the Commission maintain the confidential version of the testimony under seal and protect the same from disclosure until such time as the Commission has ruled on any motion which SCE&G may file.

Thank you in advance for your consideration of this request.

Sincerely,



E. Wade Mullins, III

Damon E. Xenopoulos, Esquire
Brickfield, Burchette, Ritts & Stone, P.C.
1025 Thomas Jefferson Street, N.W.
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Washington, D.C. 20007

Counsel to CMC Steel

PUBLIC VERSION

**DIRECT TESTIMONY OF
RICHARD THOMAS
ON BEHALF OF
CMC STEEL SOUTH CAROLINA
DOCKET NO. 2009-2-E
IN RE: ANNUAL REVIEW OF BASE RATES FOR FUEL COSTS
OF SOUTH CAROLINA ELECTRIC & GAS COMPANY**

INTRODUCTION AND QUALIFICATIONS

Q. PLEASE STATE YOUR NAME, OCCUPATION, AND ADDRESS.

A. My name is Richard Thomas. I operate as an independent consultant. My address is 26 Cold Spring Road, Monroe, CT 06468.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL BACKGROUND.

A. I received a Bachelor of Science in Civil Engineering from the University of Arizona. I was Manager Fuels Purchasing for Metropolitan Edison Company and Martin Marietta Cement from 1973 through 1979. I sold coal for C&K Coal Company from 1979 through 1980. I traded coal internationally for CTC-Minemet and Intercarbo from 1980 through 1997. I helped develop the Over-the-Counter coal trade for Natsource, LLC beginning in 1997.

During my career, I have been responsible for the purchase of coal and other energy products, the coordination of the transportation of these products both domestically and internationally, the monitoring of quality control, the processing of the products, and the direct as well as brokered sales of coal. I have consulted with producers as well as domestic and international energy traders.

Q. ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?

A. I am appearing on behalf of CMC Steel South Carolina, a member of CMC Steel Group.

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1 **Q. WHAT ASSIGNMENT WERE YOU GIVEN WHEN YOU WERE**
2 **RETAINED?**

3 A. I was asked to undertake two primary tasks:

- 4 1. Review 2008 coal purchases made by South Carolina Electric & Gas
5 Company ("SCE&G" or "Company").
- 6 2. Identify any imprudent purchases or policies, and suggest recommended
7 changes.

8 **Q. WHAT SPECIFIC INFORMATION DID YOU REVIEW IN**
9 **CONDUCTING YOUR EVALUATION?**

10 A. I reviewed SCE&G's filing, testimony, exhibits, and responses to requests for
11 information. I also reviewed information found on web sites operated by the
12 Commission, and by SCE&G and its parent-SCANA Corporation. In addition, I
13 reviewed what was purported to be all SCE&G spot and long-term coal
14 purchasing contracts in effect during 2008.

15 CONCLUSIONS

16 **Q. WHAT CONCLUSIONS HAVE YOU REACHED?**

17 A. On the basis of my review and evaluation, I have concluded the following:
18 1. During 2008, SCE&G's fuels purchasing personnel faced difficult
19 market conditions characterized by extremely volatile prices. By Company
20 policy, these personnel were not authorized to use financial hedging tools that
21 could have mitigated the effect of these volatile prices on the Company's fuel
22 costs. *See* Exhibit __ (RT-1). Coal-fired generation is an important part of the
23 base load of SCE&G. Each year, the Company can forecast, with reasonable
24 accuracy, the coal needs for the following years. In his Direct Testimony,
25 Gerhard Haimberger testifies that these needs are met by long-term contracts

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1 (one third of which are rolled each year) and spot purchases for the balance of
2 their needs. The portion of the long-term contracts due for replacement in any
3 year, and the spot purchases for that year should be hedged well before the
4 beginning of the year. Financial hedges can be accomplished by forward OTC
5 purchases, financial swaps, call options, or other means. A swap is defined as
6 a financial transaction between two parties to exchange a fixed price for a
7 floating price at some fixed date in the future. The buyer of the swap will
8 receive financial payment if the price of the commodity increases. This
9 payment can be used to offset the increased price of the commodity if it is then
10 purchased.

11 If SCE&G had financially hedged coal purchases for 2008 during the middle
12 of 2007, it could have done so using the CSX 1% swap and forward markets
13 that were at approximately \$47.50 (July 2007 OTC trades)¹. [REDACTED]

14 [REDACTED]

15 [REDACTED]

16 [REDACTED]

17 [REDACTED]

¹ As evidenced by OTC coal trades as well as forward market assessments reported in Argus Coal Daily Coal Trade Summary, Platts Coal Trader, and Energy Publishing Coal and Energy Price Report. See Exhibit __ (RT-2). In addition, the attached NYMEX settlement levels for contract QX provide evidence of this approximate level of \$47.50. See Exhibit __ (RT-3).

[REDACTED]

[REDACTED]

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[REDACTED]

RECOMMENDATIONS

15

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Q.

**WHAT DO YOU RECOMMEND ON THE BASIS OF THESE
CONCLUSIONS?**

17

18

A.

1. I recommend that SCE&G immediately institute a financial hedging program that protects their rate payers from adverse price movements in future coal purchases. This program should include all available hedging tools, including but not limited to financial swaps, options, and forward OTC purchases. A financial hedging program can be implemented that will contain price spikes for the current year and at least two years forward, given existing tools.

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1 In his Direct Testimony, page 9, Company witness Gerhard Haimberger
2 testifies that SCE&G renegotiated certain contracts because "it could not
3 determine when or if prices may moderate". It is precisely for this reason that
4 financial hedging should be a part of SCE&G's coal purchasing program.

5 [REDACTED]
6 [REDACTED]
7 [REDACTED]
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17 [REDACTED]
18 [REDACTED]
19 [REDACTED]

20 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

21 **A. Yes.**

**SOUTH CAROLINA ELECTRIC & GAS COMPANY
CMC STEEL SOUTH CAROLINA'S FIRST SET OF DATA REQUESTS
DOCKET NO. 2009-2-E**

QUESTION NO. 1-12

Regarding SCE&G's responses to CMC discovery requests in Docket No. 2008-302-E, especially CMC 1-9, explain in detail SCE&G's position and use of financial hedges in relation to its coal purchasing practices. (In response to CMC 1-9, SCE&G wrote "The Company does not believe that financial hedges are appropriate to institute as part of its coal purchasing practices.")

ANSWER NO. 1-12

The Company does not believe that financial hedges are appropriate to institute as part of its coal purchasing practices.

July 2007 Rail OTC Coal Trades
As Reported by Argus Coal Daily
www.argusmedia.com

| Trade Date | Product* | Term | Volume | Price |
|------------|-----------|----------------|--------|---------|
| 7/3/2007 | NS 1% | Cal 08 | 120000 | \$48.00 |
| 7/11/2007 | CSX 1% | July 07 | 20000 | \$41.50 |
| 7/11/2007 | CSX 1% | Q3 07 | 30000 | \$42.00 |
| 7/11/2007 | CSX 1% | Q3-Q4 08 | 60000 | \$48.35 |
| 7/12/2007 | CSX 1% | Q3 07 | 30000 | \$42.00 |
| 7/12/2007 | CSX 1% | Cal 08 | 120000 | \$47.50 |
| 7/12/2007 | CSX 1% | Cal 08 | 120000 | \$47.50 |
| 7/12/2007 | CSX 1% | Cal 08 | 120000 | \$47.50 |
| 7/12/2007 | CSX 1% | Cal 08 | 120000 | \$47.50 |
| 7/16/2007 | CSX 1% | Cal 08 | 120000 | \$47.15 |
| 7/17/2007 | NS/CSX 1% | Cal 08 | 240000 | \$1.15 |
| 7/17/2007 | CSX 1% | Aug-Sep 07 | 20000 | \$42.00 |
| 7/17/2007 | CSX 1% | Aug-Sep 07 | 20000 | \$42.00 |
| 7/17/2007 | CSX 1% | Cal 08 | 120000 | \$47.15 |
| 7/23/2007 | CSX 1% | Q1-Q2 08/Q4 07 | 120000 | \$2.15 |
| 7/24/2007 | CSX 1% | Cal 08 | 120000 | \$45.50 |
| 7/25/2007 | CSX 1% | Aug-Sep 07 | 20000 | \$41.75 |
| 7/31/2007 | CSX 1% | Cal 08 | 120000 | \$46.50 |

* NS refers to coal originating in the Thacker or Kenova Dist, Norfolk Southern RR
CSX refers to coal originating in the Big Sandy or Kanawha Dist, CSX RR
1% refers to coal with 12,500 BTU/lb and 1% Sulfur

NY Mercantile Exchange Settlements for July, 2007 - CSX 12500 BTU, 1 % Sulfur (NYMEX Contract QX)
(see http://www.nymex.com/settle_fut_otc.aspx)

| Settlement Date | Product | Term | Avg Settle Price |
|-----------------|---------|--------|------------------|
| 7/10/2007 | QX | Cal 08 | 46.50 |
| 7/11/2007 | QX | Cal 08 | 46.30 |
| 7/12/2007 | QX | Cal 08 | 47.50 |
| 7/13/2007 | QX | Cal 08 | 47.50 |
| 7/16/2007 | QX | Cal 08 | 47.15 |
| 7/17/2007 | QX | Cal 08 | 46.89 |
| 7/18/2007 | QX | Cal 08 | 46.74 |
| 7/19/2007 | QX | Cal 08 | 46.84 |
| 7/20/2007 | QX | Cal 08 | 46.56 |
| 7/23/2007 | QX | Cal 08 | 45.51 |
| 7/24/2007 | QX | Cal 08 | 45.46 |
| 7/25/2007 | QX | Cal 08 | 45.68 |
| 7/26/2007 | QX | Cal 08 | 45.83 |
| 7/27/2007 | QX | Cal 08 | 46.15 |
| 7/30/2007 | QX | Cal 08 | 46.40 |
| 7/31/2007 | QX | Cal 08 | 46.40 |

**BEFORE THE
SOUTH CAROLINA PUBLIC SERVICE COMMISSION**

Docket No. 2009-2-E

In RE:

**Annual Review of Base Rates for Fuel
Costs of South Carolina Electric and Gas
Company**

CERTIFICATE OF SERVICE

This is to certify that I have caused to be served this day a copy of the **Direct Testimony** of **Richard Thomas on behalf of CMC Steel South Carolina** via first-class mail, postage pre-paid, to the persons named below at the addresses set forth below:

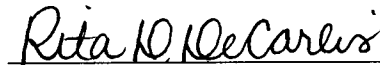
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